

BEFORE THE  
FEDERAL COMMUNICATIONS COMMISSION  
WASHINGTON, D.C. 20554

In the Matter of:

FCC 2000 Biennial Regulatory Review  
Accounting and Reporting  
Requirements for Incumbent Local  
Exchange Carriers

CC Docket No. 00-199  
CC Docket No. 97-212  
CC Docket No. 80-86  
FCC Docket No. 01-305

**MOTION  
TO ACCEPT LATE-FILED COMMENTS  
(COMMENTS ATTACHED)**

The California Public Utilities Commission (California or CPUC) respectfully submits this Motion to Accept Late-Filed Opening Comments in the above docket, FCC 2000 Biennial Regulatory Review Accounting and Reporting Requirements for Incumbent Local Exchange Carriers. The Federal Communications Commission (FCC) NPRM was printed in the Federal Register on February 6, 2002, and the Federal Register published the dates to respond to the NPRM. The CPUC's Opening Comments were due on April 8, 2002.

Urgent situations at the CPUC have resulted in a shortage of CPUC staff resources. Consequently, the CPUC was unable to prepare and submit its Opening Comments by April 8, 2002. We ask the FCC to accept these late-filed Opening

Comments in the above docket, FCC 2000 Biennial Regulatory Review  
Accounting and Reporting Requirements for Incumbent Local Exchange Carriers.

Respectfully submitted,

GARY COHEN  
HELEN MICKIEWICZ  
LIONEL WILSON  
GRETCHEN DUMAS

By: /s/ GRETCHEN DUMAS

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GRETCHEN DUMAS

Attorneys for the  
Public Utilities Commission  
State Of California

505 Van Ness Ave.  
San Francisco, CA 94102  
Phone: (415) 703-1210  
Fax: (415) 703-4432

April 30, 2002

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COMMENTS OF THE PEOPLE OF  
THE STATE OF CALIFORNIA AND THE  
PUBLIC UTILITIES COMMISSION OF THE  
STATE OF CALIFORNIA

GARY M. COHEN  
HELEN M. MICKIEWICZ  
LIONEL B. WILSON  
GRETCHEN T. DUMAS

Attorneys for the  
Public Utilities Commission  
State Of California

505 Van Ness Ave.  
San Francisco, CA 94102  
Phone: (415) 703-1210  
Fax: (415) 703-4432

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COMMENTS OF THE PEOPLE OF  
THE STATE OF CALIFORNIA AND THE  
PUBLIC UTILITIES COMMISSION OF THE  
STATE OF CALIFORNIA

The People of the State of California and the Public Utilities Commission of the State of California (California) respectfully submit the following comments regarding the 2000 Biennial Regulatory Review – Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers: Phase 2.<sup>1</sup> With this rulemaking, the FCC proposes to make “fundamental changes to the accounting and reporting requirements,” and it

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<sup>1</sup> In 1999, the FCC initiated a two-phased comprehensive review of its accounting rules and the related reporting requirements for incumbent local exchange carriers (“ILECs”) to keep pace with changing conditions in a competitive telecommunications industry. In its first Report and Order in CC Docket No. 99-253, (“*Phase 1 Report and Order*”), adopted March 2, 2000 and released March 8, 2000, the FCC approved accounting rule changes and reporting reform measures for the Automated Reporting Management Information System (“ARMIS”). Later, on October 11, 2001, the FCC adopted another Report and Order (FCC 01-305) in CC Docket Nos. 00-199, 97-212, and 80-286, (“*Phase*

seeks comments on whether these requirements, to the extent they survive, should be sunsetted by “a date certain.”<sup>2</sup> In addition to seeking comment on sunsetting the remaining Class A accounts by a date certain, the FCC seeks comment whether ARMIS information (particularly infrastructure data) would be better captured through the Local Competition and Broadband Data Gathering Program rather than in ARMIS, whether the rules for continuing property records (CPR) and the affiliate transactions rules for price cap carriers should be eliminated, and whether conforming the separations rules to any changes to the chart of accounts in the Report and Order is necessary.<sup>3</sup>

The FCC’s review of these accounting and reporting requirements is premised on the assumption that competition is developing to a degree which may invalidate “the original justifications for the Commission’s accounting and reporting requirements....”<sup>4</sup> The Commission explains that it is moving ahead to eliminate these accounting and reporting requirements despite the fact that “state

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2 *Report and Order*”) which imposed additional and significant revisions to streamline Parts 32 and 64 of the FCC’s rules. These reductions were based on FCC determinations that the specific accounting rules/reports involved were no longer necessary or were outdated in the FCC’s “pro-competitive, deregulatory” national policy framework for the telecommunications industry. Concurrently with the *Phase 2 Report and Order*, the FCC initiated a *Further Notice of Proposed Rulemaking* seeking comment on, *inter alia*, the appropriate circumstances for eliminating accounting and reporting requirements, whether certain ARMIS data is more appropriately collected through other means; and how to amend the separations rules to reflect modifications to the Uniform System of Accounts.

<sup>2</sup> “Notice of Proposed Rulemaking,” Federal Register, Vol. 67, No. 25 [CC Docket Nos. 00-199, 97-212, and 80-286; FCC 01-305].

<sup>3</sup> Ibid.

<sup>4</sup> Ibid., p. 5705.

regulators have articulated current regulatory needs to maintain certain Class A accounts and ARMIS filing requirements for various purposes, including assisting their work in promoting local competition, developing appropriate prices for unbundled network elements, and conducting local ratemaking proceedings.”<sup>5</sup>

Notwithstanding these concerns that the states have articulated, the FCC still seeks to move forward with these proposed actions, because it assumes that if it “cannot identify a federal need for a regulation, it is not justified in maintaining such a requirement at the federal level.”<sup>6</sup> Therefore, the FCC states that it would like to work with the states to arrange an orderly transition to a mechanism in which states undertake responsibility for gathering data.

## **I. SUMMARY**

California believes that a national system of accounting requirements is in the public interest. Moreover, the states’ needs in the accounting area should be respected even if the FCC no longer has a specific need for these records. The accounts that the FCC’s rules should continue to require the ILECs to maintain, if states still need them, are Class A Uniform System of Accounts, Part 32, ARMIS Requirements, Affiliate Transactions Rules and Continuing Property Records.

California further notes that as we move towards a competitive market, accounting and reporting requirements should be the last set of federal regulatory

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<sup>5</sup> Ibid.

<sup>6</sup> Ibid.

requirements affecting ILECs to be eliminated. Moreover, such requirements should be removed only after there is clear and incontrovertible evidence that doing so would be in the public interest. At this time, California does not believe that the limited amount of competition in local telephone exchanges warrants the type of actions called for in this NPRM.

To justify the actions contemplated by the FCC in this docket, the level of existing competition must be sufficient to prevent abuse and anti-competitive practices by the ILECs. Accounting requirements are a major tool in exposing such behavior, and the elimination or modification of such requirements would increase the potential for abuse and anti-competitive practices. However, because the level of competition in residential local telephone markets is still very limited, and because the potential for abuse and anti-competitive practices is still substantial, it would be a grave mistake for the FCC to eliminate a major remaining tool to keep the potential for anti-competitive behavior in check.

Thus, California does not believe that it is in the public interest to deregulate accounting and reporting requirements on certain set dates in the future without a finding based on clear and incontrovertible evidence that eliminating such accounting requirements would be in the public interest.

## **II. THE CONTINUING NEED FOR FEDERAL ACCOUNTING RULES**

### **A. FCC's Premise Regarding Competition Is Inaccurate**

While the FCC's documentation in support of its proposed rulemaking makes the assertion that significant competition exists to warrant such extreme changes to the federal accounting rules, the documentation does not supply any evidence to support that premise. Therefore, any regulatory action stemming from that premise would be dubious at best.

For instance, from the point of view of residential users of telecommunication services, there is in fact precious little competition. ILECs retain market shares in excess of 90% in almost every jurisdiction in the country. In California, SBC Pacific Bell ("Pacific") retains a market share in excess of 94%; Pacific's high-speed data affiliate has in excess of 700,000 DSL customers;<sup>7</sup> no DSL competitor has even 2% of this number of customers in California. Moreover, by Pacific's own admission, its market share for DSL in California runs ahead of the market share for cable modem access by a significant margin, with DSL having over 51% of the broadband access market, and cable about 44%.<sup>8</sup>

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<sup>7</sup> As of March 2002, SBC Pacific Bell claims to have 764,000 Digital Subscriber Lines in service. See "SBC Pacific Bell, Presented by the Regulatory and Constituency Relations Team," March 2002, p. 17.

<sup>8</sup> According to figures submitted by Pacific in the CPUC's Line Sharing Proceeding, July 2001.

According to the California ISP Association, Pacific's internet services off shoot, ASI, controls over 90% of the market for DSL transport in the state.<sup>9</sup>

Thus, rather than seeing a healthy development of competition for advanced telecommunications services, such as DSL, the opposite seems to be happening: the ILEC dominance of the local exchange market is being matched by ILEC dominance in the provision of advanced telecommunications services.

The FCC's premise that significant competition exists may be even less true in the future. Recent observers have speculated on the narrowing of competitive options in the long distance market as the RBOCs enter that field. Many of these same observers have noted the likelihood of the RBOCs purchasing surviving long distance companies and thereby gaining not only the long distance market share of those companies but combining it with whatever market share they have quickly gained via the Section 271 route.<sup>10</sup>

If, as explained above, the FCC's "competition development" premise is wrong, the existing federal accounting and reporting requirements become all the more important for tracking the activities of these burgeoning regional monopoly providers in local exchange service, broadband access, and long distance. Thus, the FCC's proposed truncation of federal accounting and reporting requirements will ironically coincide with the collapse of competition, not its development, and

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<sup>9</sup> Complaint O1-070-027, California ISP Association vs. Pacific Bell; SBC Advanced Solutions Inc., March 13, 2002.

<sup>10</sup> See for instance, [Will Ma Bell Be Taken Over by Offspring?](#) By SETH SCHIESEL (NYT) News New York Times Online Edition, April 1, 2002.

will have the effect of undermining, rather than supporting, the growth of a healthy, functioning competitive marketplace for advanced telecommunications services.

**B. When Competition Finally Exists, Accounting Requirements Will Still Be Needed.**

The premise that “significant competition exists” on which the FCC rests its rationale in this docket may be faulty in another sense. The assumption that competitive markets do not require accounting and reporting safeguards is inaccurate. The high profile accounting scandals of recent months support more government oversight and more regulated utilities, rather than less. Thus, even if one were to assume that a more competitive market exists today for telecommunication services than is actually the case, there is no reason or need to lessen regulatory scrutiny over telecommunications service providers.

Rather, the opposite is the case. Markets are vulnerable to failures of honest accounting and full reporting, and they certainly remain vulnerable to residual monopoly market power. It is counterintuitive to embrace the principle of open markets without embracing the commensurate requirement for open books and full disclosure. The elimination of the accounting requirements such as USOA, ARMIS, Affiliate Transactions Rules, and CPR will raise uncertainties about, and may well compromise the integrity, of the financial information provided to state and federal regulators at a time when the integrity of financial reporting is crucial to sustainable economic growth and to the confidence the

American people must have in the viability of the public utilities upon which they depend.

Finally, recent events regarding the accounting practices of energy and telecommunications companies and the selective auditing practices of certain accounting firms should forcefully bring home to the FCC that this is clearly not the time to relax accounting rules and accountability. Indeed, the FCC should be doing the opposite. The formal system of accounting requirements and controls now in place reduce the possibilities of hidden liabilities, overstated assets remaining undetected, and discourages “creative” accounting, where accuracy is secondary to inventiveness.

**C. The States’ Needs in the Accounting Area Should Be Considered Even If There Is No Longer a Federal Need for These Records**

The proposed rulemaking concedes that states may continue to need Uniform System of Accounts, Class A, Part 32 and ARMIS filings in their efforts to promote local competition, fix appropriate prices for unbundled network elements, and conduct local ratemaking proceedings. Indeed, the FCC proposes to allow the states sufficient time to adjust to the disappearance of these accounting and reporting requirements at the federal level because of the “severe problems for state regulators” their absence would create.<sup>11</sup> The premise of this reasoning, again unsupported in the rulemaking itself, is that the FCC, at the federal level, has

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<sup>11</sup> NPRM, FR at 5705.

no continuing need to promote local competition or the correct pricing of unbundled network elements (not to mention the identification of unbundled network elements), or to track local rates and local revenues. It is odd, certainly, that a recognition of the need for continuing *state* regulation of what are *national* and *regional* monopoly providers of local exchange service and broadband access is so casually detached from any recognition of a federal role in such regulation. The detachment is assumed, not argued, and it is made without any concession to state authority regarding federal jurisdiction over interstate telecommunication services.

No specified amount of time, whether three years, five years or even ten years, may be enough to overcome the fact that states are expected to regulate national and regional monopolies without any effective federal assistance. It is one thing for the federal government to propose blinding itself to the market power and actions of *nationally based* incumbent local exchange carriers, even as these carriers are becoming distinctly unlocal in their behavior, but it is quite another to propose that states be rendered equally sightless regarding activities that are national or regional in scope, and upon which the provision of local services are dependent.

Already in California we have seen the effect of SBC's movement of services and personnel to its national corporation (administrative services, operations services, and advanced services, for instance) so that fewer activities of

the company's state entity, SBC Pacific Bell, are "local" in character. **Cite to NRF AUDIT.** The development that should be of concern to the FCC is the transformation of incumbent local exchange carriers into giant regional or sub-national monopolies, into which the local operating companies that were traditionally regulated on the state level are wholly absorbed, such that what remains local is only a "brand" name, not an independent state entity. Even that is changing in California as SBC is sending out bills with return addressee to identified as "SBC Pacific Bell".

Further, throughout the text of the rulemaking, the FCC frequently frames the issues in terms of the "substantial burdens [placed] on incumbent LECs."<sup>12</sup> A more prudent and proper way of framing this would be to assess the burdens in terms of the scope of market power the incumbent LECs exercise. The size of the burden should be proportionate to the size of the market dominance. With success come responsibility and its associated burdens. This is as it should be.

### **III. CLASS A UNIFORM SYSTEM OF ACCOUNTS, PART 32**

The Class A Uniform System of Accounts ("USOA"), a proven system, should continue to be a requirement for the RBOCs. The USOA standardizes the accounting and reporting requirements across different jurisdictions. It is invaluable for performing financial comparisons and operation analyses. The USOA serves as the starting point for regulatory audits for which there is an

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<sup>12</sup> NPRM, FR 5706.

ongoing need, both at federal and state levels. The USOA system of accounting requirements and control now in place tends to reduce the possibilities of hidden liabilities and overstated assets remaining undetected. This regulatory system of accounting controls tends to discourage “creative” accounting, where accuracy is secondary to creativity, and other questionable accounting practices that would be against the public interest.

#### **IV. ARMIS REQUIREMENTS**

California considers the ARMIS reports an invaluable source of information for comparison and benchmarking purposes. This system of reports has been an important source of service quality information for California. If these reports were eliminated, state regulators would have no comparable source of information that is nationally based, and neither California, nor any other state on its own, could generate such a national reference base. A key feature of the ARMIS system is that reports are available at the FCC website, thus making the information available instantaneously to state regulators and other researchers. Another important feature of the ARMIS reports is that the information is reported and displayed in a consistent manner for all carriers. Because of this consistent data base arrangement, federal and state regulators can assess performance over a period of time and gauge the direction of changes, their geographic locus, and can distinguish type of service dynamics.

States have used ARMIS in assessing the service quality performance of carriers in the state as well as making interstate comparisons. Consumers can also benefit by using the service quality information in ARMIS to make informed choices among competing carriers. The ARMIS reports contain information about installations and repair intervals, as well as the results of customer opinion surveys. It is from this source that a state can learn that the dominant carrier in its jurisdiction has a poor repair service record. As a result, state regulators have relied on ARMIS reports for many years. Moreover, state regulators will continue to have need for the information contained in these reports into the foreseeable future.

If the FCC ignores the concerns expressed by NARUC and the state regulators in this docket and proceeds with the dismantling of the ARMIS system, California recommends that a federal/state joint committee be established to explore the possibility of transferring the function and maintenance thereof to the National Regulatory Research Institute under the oversight and authority of a federal/state joint board. Funding for any such new operation should be assessed by the FCC against the respondent carriers for a minimum of ten years.

## **V. AFFILIATE TRANSACTION RULES**

Affiliate transaction rules should remain in place and not be eliminated until there is a finding of effective competition in the marketplace. Affiliate

transaction rules protect ratepayers from possible cross-subsidies occurring from transactions between ILECs and their affiliates. Without these rules, regulators will not be able to uphold their statutory obligation under the 1996 Act to diminish cross-subsidization of potentially competitive services.

Specifically, affiliate transaction rules and associated reporting requirements are needed because in the past, regulatory audits of major carriers have revealed substantial non-compliance with these rules. For example, the transfer of an affiliate's marketing function to an ILEC creates the possibility that telephone company customer data will be made available to non-regulated affiliates for marketing purposes. If this were to actually happen, the ILEC could confer a competitive advantage on its non-regulated affiliates. Such a troublesome and problematic result would lead to less competition, not more, competition in the telecommunication's marketplace.

## **VI. CONTINUING PROPERTY RECORDS**

California believes that sunseting Continuing Property Records (CPRs) by a date certain, whether or not there is effective competition, does not make sense. More specifically, CPRs are needed, because they deal with the largest and most important accounts of ILECs, namely, their network plant accounts, and they accurately reflect those assets actually in-service. In an environment when competitors are still largely dependent on the incumbent provider and its facilities to provide service, CPRs provide the only real record of the history of the existing

facilities. Also, CPRs provide data for jurisdictional separations and cost allocations studies as well as for the FCC to update its depreciation life and salvage ranges.

Moreover, these records provide the basic information used as the beginning point in forward-looking pricing models. To the extent that the proxy model utilizes historical relationships based on erroneous data to determine forward-looking plant specific expense and other expense categories, interstate universal service support for nonrural ILECs may be affected. In establishing any state Universal Service Fund (“USF”), use of erroneous embedded data similarly may result in misstatements of funding requirements, if estimates of expense levels attributable to universal service are based on faulty historical cost relationships. In either event, the reliance on historical costs that are misstated could mean the calculations used to establish a state USF may be inaccurate. Furthermore, CPRs are also used in valuations of property for sales and mergers as well as for property tax assessments.

Eliminating CPR rules outright will create a situation fraught with problems. If CPR requirements are eliminated, it is highly unlikely that alternative information sources, useful to state regulators, would be developed. Even if such information were available, state regulators would be required to make annual, special requests to each ILEC for the information that they need. Under these

conditions, it is unlikely that the information would be consistent from ILEC to ILEC nor is it likely that it would be consistent from one year to the next.

CPRs represent the guideline framework for capitalization and expensing procedures. Without CPR rules, ILECs could change the procedures depending on financial conditions.

The FCC noted that ILECs have an incentive, for engineering purposes, to track their property at the unit level, whether it is cable or the detail components of their various types of switches [*Report and Order* 01-305, ¶ 211] While this is generally true, the information is in a format required by the engineering systems, and not in a format that is useful for performing financial analysis of the data or reviewing costs. The ILECs generally do not have an incentive to track their cost at any level of detail, except for specific projects. Further, if there is no formal requirement to produce the information on a periodic basis, the information needed by regulators will only be produced on a formal request basis. This will make it difficult for the regulator to get a clear understanding of how the investment is evolving over time and to detect any unusual changes in investment.

Moreover, the CPRs have major value for *national and homeland security purposes*. Since, the CPRs provide the detailed support essential to the ubiquitous telecommunications infrastructure, in the event of or in anticipation of a major catastrophic event, the CPRs would provide crucial details such as locations of sensitive, strategic or vulnerable facilities in the nation telecommunications system

(types of facilities, location maps, etc.), thus facilitating security preparation. This information would also aid in any reconstruction or emergency repair efforts to restore telecommunications services in the event of a catastrophe. Moreover, the CPRs would aid in any request by the telecommunications utilities for financial assistance or compensation. The CPRs would clearly serve as a starting point for cost determination in that regard.

In view of growing concerns and mistrust over published financial statement and accounting information, the elimination of the CPR requirements would be contrary to the public interest. Thus, in addition to its other values noted above, the CPR system serves as a control and support mechanism for plant investment. Its elimination would remove a major accounting control for such investment, which is generally the largest monetary item on a telecommunications utility's balance sheet.

## **VII. CONCLUSION**

In conclusion, FCC's proposed dismantling of the ARMIS reporting system, downsizing of the uniform of system of accounts requirements, and the elimination of the CPRs and affiliate transaction rules are clearly adverse to the public interest and should not be adopted. The present lack of real or effective competition to the ILECs should serve as a warning. The ongoing mergers and acquisitions by the few dominant carriers, the centralization of corporate functions by the dominant carriers, alliances and relationships among competing carriers, the

commingling of regulated and non-regulated activities – all these should heighten the need of state and federal regulators to enforce accounting safeguards and reporting requirements, not the reverse.

Respectfully submitted,

GARY M. COHEN  
HELEN M. MICKIEWICZ  
LIONEL B. WILSON  
GRETCHEN T. DUMAS

By: /s/ Gretchen T. Dumas

---

Gretchen T. Dumas

Attorneys for the  
Public Utilities Commission  
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505 Van Ness Ave.  
San Francisco, CA 94102  
Phone: (415) 703-1210  
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